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No. 82-2091

IN THE
Supreme Court of the United States
OCTOBER TERM, 1982

SHEARN MOODY, JR.,
Petitioner,

v.

DAVID C. MEYERS, *et al.*,
Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

MOTION FOR LEAVE TO FILE BRIEF OF AMICI CURIAE, AND BRIEF OF AMICI CURIAE, THE AMERICAN CONSERVATIVE UNION AND THE CONSERVATIVE CAUCUS, INC., IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

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MOTION FOR LEAVE TO FILE BRIEF OF AMICI CURIAE, THE AMERICAN CONSERVATIVE UNION AND THE CONSERVATIVE CAUCUS, INC., IN SUPPORT OF PETITIONER

The American Conservative Union and The Conservative Caucus, Inc., hereby respectfully request leave to file the attached Brief of Amici Curiae in support of the Petition for Writ of Certiorari in this case.

Amicus American Conservative Union is a non-profit, tax-exempt corporation organized and existing under the

laws of the District of Columbia. It has forty-three state affiliates, and more than 325,000 members, contributors, and supporters throughout the United States whose interests the ACU represents. The ACU, among other goals, is concerned with lessening of the burdens of government and promoting the principles of federalism, including the maintenance of the proper relation between the federal courts and the governmental agencies of the fifty states. The ACU also supports the principles of the free enterprise system, including a rational system of corporate governance and responsibility which will not unduly impede the continued development of our system of private enterprise.

Amicus Conservative Caucus, Inc., is a non-profit organization founded in 1974 to advance various conservative policy objectives. With over 400,000 supporters, the Conservative Caucus is one of the largest conservatively oriented "grass roots" lobbying organizations in the country. The Conservative Caucus is currently engaged in a major project to develop and promote legislative proposals for reform of the federal judicial system. This project focuses, *inter alia*, on issues relating to the relationship between federal and state courts. Amicus is therefore highly interested in the issues presented by the Petitioner.

Accordingly, amici respectfully request that they be permitted to state their views on the merits of the Petition. Amici will show that the decision of the Fifth Circuit in this case is an impermissible collateral attack on the lawful determinations of a state Insurance Commissioner, of a type prohibited by the laws of the states concerned. Authorities and policy arguments not contained in the Petition, but relevant to the issues presented therein, will be discussed. The brief will also show that the Fifth Circuit's decision imposes corporate fiduciary

liability based upon principles which are contrary to state law and without basis in policy.

Respectfully submitted,

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STATEMENT

Amici adopt the statement of Petitioner. Pet. 2-6.

INTEREST OF AMICI

The interest of Amici is set forth in the foregoing Motion.

SUMMARY OF ARGUMENT

The decision of the Fifth Circuit Court of Appeals, if allowed to stand, will seriously undermine the ability of state administrative agencies to regulate matters which are entrusted to them, by allowing agency determinations to be collaterally attacked in subsequent federal court proceedings. In the exercise of their business judgment, corporate officers and directors of regulated companies must be able to rely upon the adjudications of the agencies which regulate their companies' affairs. If the determinations of these agencies—which are binding on the companies and their officers and directors during the time they are in effect—can later be disregarded by the federal courts, there will be no rational basis for business planning and a wholly unwarranted increase in personal liability of officers and directors will result. The sole basis upon which the Fifth Circuit predicated liability involved just such a collateral attack.

The Court said that "there was only one wrong complained of and proved: the manipulation of the life interest leading to fatal undercapitalized acquisition * * *." Pet. App. 27. Yet the valuation of the life interest of which the Fifth Circuit complains was placed on it by the Alabama Insurance Department, and the subsequent acquisitions of other insurance companies in reliance on that valuation were also approved by the Department. The Fifth Circuit, in disregarding these facts, has rendered the actions and findings of the Alabama Insurance Department nugatory. Under the rules of law prevailing in Alabama and Texas, as well as in other states and throughout the federal system, it is clear that a binding adjudication of a state agency is not subject to collateral attack in the form of a suit for damages. But precisely that has occurred in this case.

The Alabama Insurance Department has a duty to make an independent decision regarding the affairs of the insurance companies which it regulates, and in this case it did so. There are no permissible legal grounds for a collateral inquiry into the merits of that decision. Though the basis for the Fifth Circuit's disregard of the Department's findings is unclear, nothing in the case remotely approaches extrinsic fraud, which is the only basis under state law for a collateral attack.

When a regulatory agency has made a decision which is binding upon the regulated company, the officers and directors of that company must be able to rely upon it without fear of liability. It is well established that corporate directors may rely upon the opinions of counsel, accountants, and other experts in making corporate decisions. In the area of insurance, there should be no one more expert than the public officials charged with making determinations regarding the assets, liabilities, and other financial affairs of insurance companies. The trend in state and federal decisions pertaining to fiduciary responsibilities of corporate officers and directors has been to increase their ability to rely upon impartial, outside advice. The argument of the Fifth Circuit—that a company cannot "delegate" its responsibility to value its assets—has no basis in law or reason. Alabama and Texas law expressly place on insurance department officials the duty to value the assets of insurance companies. This is no more than a recognition of the established rule that such delegation comes from the legislature, not from the regulated company. Because the legal linchpin of the Fifth Circuit's decision is a principle which has no basis in policy, and runs directly counter to applicable state law, certiorari should be granted and the decision reversed.

ARGUMENT

I. THE DECISION OF THE FIFTH CIRCUIT IS AN IMPERMISSIBLE COLLATERAL ATTACK IN VIOLATION OF STATE LAW WHICH USURPS THE POWER OF THE STATES TO ADMINISTER THEIR INSURANCE LAWS.

Stripped to its essence, the contention of the Receiver in this case is truly remarkable. It is unquestioned that when Shearn Moody, Jr. was an officer and director of the Empire Life Insurance Company, and the company requested the Alabama Insurance Department to revalue an asset, the Department did in fact do so, placing on it a valuation close to one value submitted by Empire. That valuation was confirmed by a subsequent Superintendent of Insurance. Acquisitions of other insurance companies—in reliance upon the Superintendent's valuation—were also approved by the Department. *See* Pet. 14 (giving citations to the record). Now the present Commissioner contends that those determinations made by his predecessors were erroneous, and that Moody should be held personally liable for actions taken in reliance thereon during the time the determinations were in effect.

A lawsuit which predicates liability upon the theory that the life interest was not worth what the Department of Insurance said it was, and that the acquisitions should not have taken place despite approval by the Department of Insurance, is clearly a collateral attack. Liability in this case was predicated only on state law, and on most questions the Fifth Circuit applied the law of Texas. Pet. App. 19, 26. The Texas courts have applied the following definition: "A collateral attack on a judgment is an attempt to avoid its binding force in a proceeding not instituted for such purpose * * *." *Akers v. Simpson*, 445 S.W.2d 957, 959 (Tex. 1969); *Hogan v. City of Tyler*, 602 S.W.2d 555, 558 (Tex.Civ.App.—Tyler, 1980); *Kaphan v. Fidelity & Deposit Company of Maryland*, 564 S.W.2d 459, 462 (Tex.Civ.App.—Houston [1st Dist.], 1978).

This definition has also been followed in the federal courts. In applying the rule against collateral attacks on prior determinations of a state agency, a District Court defined collateral attack as "an attempt to avoid, defeat, or evade a judgment or deny its force and effect in some judicial proceeding not provided by law for the express purpose of reviewing it." *United Merchants & Manufacturers, Inc. v. South Carolina Electric & Gas Co.*, 113 F.Supp, 257, 262 (W.D. S.C. 1953), *aff'd*, 208 F.2d 685 (1953). The Court stated that "if the action has an independent purpose and contemplates some other relief or result, the action is collateral." *Id.*

Without question, the instant proceeding was not instituted for the purpose of reviewing the decision of the Alabama Insurance Department. Instead, it has an "independent purpose" and "contemplates some other relief or result," namely, recovery of damages in a civil suit. As such, it is collateral.

It is equally clear that the laws of both Texas and Alabama prohibit collateral attacks on the quasi-judicial determinations of administrative agencies. *See* cases cited in Pet. 13, 18 n.19. The Texas and Alabama rule is in accordance with the general rule prevailing throughout the country. Both Texas and Alabama provide specific, statutory procedures which are the sole means for a *direct* challenge to rulings by the Department of Insurance. Pet. 15. Any suit not following those procedures is collateral. According to Professor Davis, proceedings that courts have classified as collateral include "suits against private parties for damages" and those "challenging the validity of prior administrative action." 2 K. Davis, *Administrative Law Treatise* § 18.10 (1958).

Until now, the federal courts have been scrupulous in refusing to entertain collateral attacks on state administrative rulings. Cases in which a state Superintendent of Insurance has attempted to retroactively impose liabil-

ity for a corporation's activities which had been approved by his predecessors are understandably quite rare. But when this has been attempted, the federal courts have rejected it out of hand. The case most similar to this one on its facts is probably *Modern Woodmen of America v. Casados*, 17 F.Supp. 763 (D. N.M. 1937). In that case, the Superintendent of Insurance was attempting to collect a premium tax for past years from a corporation which had previously been determined to be a fraternal society, and thus exempt from the tax. A three-judge panel held that the prior administrative adjudications were not subject to collateral attack. The opinion is worth quoting at some length:

> Each year plaintiff was determined to be a fraternal society and licensed as such. No one throughout the years has challenged such determination. No direct attack has ever been made on any such orders of the Superintendent of Insurance. The attack here is purely collateral. What the present head of the insurance department alleges is simply that the determinations of his predecessors were erroneous, and asks this court to disregard them. This we cannot do. Where a statute reposes the decision of a question of fact in an administrative officer or body, his decision thereon, unless set aside by a court of competent jurisdiction in an appropriate proceeding, is binding on the courts in subsequent litigation. * * *
>
> Determinations of such administrative officers are generally spoken of as adjudications. Whether the term is accurate is not material; administrative officers are not judges, but in determining fact questions and entering orders based thereon, they perform judicial functions. The label is not important; the fact remains that such determinations are binding because the legislature has reposed in such officials the power to determine such facts, and orders based thereon are conclusive until they are set aside or reversed in appropriate proceedings. They are not open to collateral attacks. *Id.* at 766.

The *Modern Woodmen* case also involved a question as to sufficiency of the company's reserves. The Court's decision on reserves parallels the issue of valuation of the life interest in the present case:

> Whether plaintiff's reserves are sufficient is a question confided to the decision of the Superintendent of Insurance and his actuaries. For years, that official has approved policies issued by plaintiff with provisions for reserves, their application or withdrawal. Implicit in such approvals is a finding that the reserves met the statutory standard. Such approvals may not be collaterally attacked * * *. *Id.* at 768.

In a case in which virtually the same facts were present, a state court also applied the same rule. *State ex rel. Biel v. Royal Neighbors of America*, 44 N.M. 8, 96 P.2d 705 (1939). In holding that a determination by the Superintendent of Insurance could not be collaterally attacked, the Court noted that *for the years in question* the agency's determination is conclusive upon the taxing authorities "and all others." *Id.* at 709.

This Court, in a case applying Texas law, has affirmed that the determination of a state regulatory agency cannot be collaterally attacked in a suit against a private party for damages. In *Steele v. General Mills, Inc.*, 329 U.S. 433 (1947), the Court considered whether a motor carrier could charge the rates established by the Texas Railroad Commission, despite a contractual agreement entered into by the carrier to charge a lesser rate. The shipper set up numerous defenses, including a denial that the carrier's rates were governed by the Commission's prior rate orders. The District Court held that "Texas law barred respondent from any collateral attack on the validity of the orders", and the Supreme Court agreed. This Court noted that the determination that the orders were not subject to collateral attack was "well buttressed by state statutes and court decisions." *Id.* at 442. Be-

cause the Fifth Circuit had allowed the shipper to set up one defense which would have prevented enforcement of the rates established by the Commission, the Supreme Court reversed. The Court noted that jurisdiction was based upon diversity, and that such a defense "would result in applying a rule of law in the federal courts different from the rule we believe has been applicable in the state courts." *Id.* at 443. An argument was made in the case that allowing the Fifth Circuit's decision to stand would "impair the integrity of the State's regulatory system." *Id.* at 442. Mr. Justice Black, writing for a unanimous Court, stated that "[w]hether the Circuit Court of Appeals' judgment does undermine the transportation policy of Texas is a question of such importance that we granted certiorari to review the case." *Id.* Amici respectfully submit that the Fifth Circuit's decision in this case would equally undermine the integrity of the states' insurance regulatory systems, and that certiorari should be granted.

The lower federal courts have been equally vigilant in rejecting collateral attacks on state regulatory rulings. In *United Merchants & Manufacturers, Inc. v. South Carolina Electric & Gas Company*, 113 F.Supp. 257 (W.D. S.C. 1953), *aff'd*, 208 F.2d 685 (1953), the plaintiff brought a damages action for fraud and deceit against a utility company. In doing so, it sought to avoid the effect of certain rate rulings which had been made by the state Public Service Commission, alleging that the defendants had procured them by fraud. The Court held that the rates must be considered binding absent a direct challenge in state court. They could not be collaterally attacked in federal court.

The case of *Construction Aggregates Corp. v. Rivera de Vicenty*, 573 F.2d 86 (1st Cir. 1978), is entirely on point. In that case, the First Circuit refrained from deciding issues pertaining to rates established by the Puerto Rican State Insurance Fund. The Court doubted

whether the federal courts would even have jurisdiction, and stated:

> The laws of the Commonwealth provide for review of rates set by the Insurance Fund in the Industrial Commission, with direct review of the decision of the Industrial Commission in the Supreme Court of Puerto Rico. * * * Construction has not cited any statute or authority granting to the Puerto Rico courts jurisdiction to entertain an attack on an Insurance Fund rate in any other manner. If the laws of Puerto Rico do not recognize a cause of action permitting a collateral attack on these rates, a federal court in the exercise of its diversity jurisdiction would be unable to entertain any such claim. *Id.* at 96.

The Court went on to conclude that, even if there was jurisdiction:

> The rate-making process of the Insurance Fund is an area of intensely local interest, and judicial review of the process has been centralized in a single court. Intervention by federal courts could disrupt the efforts of the state to develop a coherent rate structure. *Id.*

Accord, *Taylor v. New York City Transit Authority*, 309 F.Supp. 785 (E.D. N.Y. 1970), *aff'd*, 433 F.2d 665 (2d Cir. 1970), "In New York State the determinations of administrative agencies acting in a judicial or quasi-judicial capacity are not open to collateral attack."); *McCulloch Interstate Gas Corp. v. Federal Power Commission*, 536 F.2d 910, 913 (10th Cir. 1976) (applying same principles to federal agencies).

Because of the importance of allowing the states full control over insurance company regulation, the federal courts have given great deference to state insurance department determinations, even when the determination is not a quasi-judicial finding of fact (as it was in this case), but is only a legal interpretation. In *United*

States v. Consumer Life Insurance Co., 430 U.S. 725 (1977), the Internal Revenue Service had assessed deficiencies against a corporation on grounds that it was not a "life insurance company" for federal income tax purposes. Qualification as a "life insurance company" depended upon how a certain liability of the company (unearned premium reserves) was to be treated. For the six years in question, the Supreme Court considered the treatment of those reserves by state insurance departments to be a "compelling" indication. *Id.* at 751. The Court noted that "[t]he insurance departments of the affected States consistently accepted annual reports showing reserves held as the taxpayers claim they should be." *Id.* In confirming the rule that such agency determinations are entitled to "great deference", the Court stated that this "is no less the rule when federal courts are interpreting state law administered by state regulatory officials * * *." *Id.* at 752. In an interesting parallel to the instant case, the Court discounted the testimony by certain insurance department officials from the states in question that the treatment of the reserves was permitted "unwittingly." *Id.* at 751, n.36. The Court rejected the notion that "this after-the-fact testimony from single officials should outweigh the formal, official approval rendered under the names of the commissioners after opportunity for full review." *Id.* Where the question is one of fact rather than law, there is even less justification for permitting a challenge to a state insurance department's determination. *See also Jordan v. Acacia Mutual Life Insurance Co.*, 409 F.2d 1141 (D.C. Cir. 1969) (deference given to interpretation by Superintendent of Insurance of *penal* statute concerning insurance companies).

In applying Texas law, the Fifth Circuit has recognized that even judgments which are plainly contrary to statute are safe from a collateral attack. *Norton v. Austin National Bank*, 557 F.2d 1061 (5th Cir. 1977). In *Norton*, the Fifth Circuit concluded that the judgment

could not be collaterally attacked, stating that "however erroneous [it] may be, [it is] not void." (*quoting Withers v. Patterson*, 27 Tex. 491, 497 (1864)). *Id.* at 1064. Since administrative adjudications are also immune from collateral attack in Texas, the Fifth Circuit had no basis in this case to pass on whether the Insurance Department's determinations were "erroneous."

In permitting the collateral attack upon the Insurance Department's determinations, the Fifth Circuit never provides any explicit statement of grounds upon which those rulings could be attacked. The opinion does contain at least two intimations that the rulings were somehow improperly obtained, but neither is sufficient to set aside an administrative adjudication.

First, the Fifth Circuit opined that Superintendent Houseal "might" have been swayed by considerations of friendship in approving the increased valuation of the life interest, since he was friends with Moody's lawyer and had visited Moody's Texas ranch on several occasions. Pet. App. 8, n.4. It is common knowledge that friendships often exist between regulators and regulated. To permit an agency action to be disregarded on such grounds would bring into question the validity of huge numbers of administrative determinations in every context. To the extent that this forms the basis for the Fifth Circuit's decision, it is wholly at variance with existing law and any concept of rational public policy.

The second ground on which the Fifth Circuit may have relied to vitiate the findings of the Superintendent of Insurance is Moody's alleged failure to disclose a subjective belief that the life interest could not be further transferred. Pet. App. 3. There is no showing that the interest was in fact not transferable, or that the alleged untransferability had any effect on the company's subsequent financial operations. But even if this fact is material from the point of view of proximate cause, which seems extremely doubtful, it is a well-settled rule of law

that quasi-judicial rulings of an administrative agency cannot be overturned on the basis of intrinsic fraud. The case of *Bolton v. Coats*, 514 S.W.2d 482 (Tex.Civ.App.—Tyler, 1974) is exactly on point. In that case, the plaintiff attempted to collaterally attack an order of the Texas Railroad Commission. The Court summarized the plaintiff's contentions, and rejected them:

> [Plaintiff] argues that since there is evidence raising the issue of whether defendants were guilty of fraud in procuring the Railroad Commission's order, defendants are estopped from relying on the order as a shield of liability. Therefore, he argues that defendants are estopped to defend themselves on the ground that his Panola County suit amounts to a collateral attack on the order. *He maintains that upon establishing the issue of fraud in the Panola County suit he would then be able to establish a breach of duty on the part of defendants* to develop the Travis Peak reservoir for oil, *irrespective of the Railroad Commission's finding* that the Travis Peak was a gas reservoir only. We find the proposition to be without merit. While we recognize that in some cases proof of the type of fraud known as extrinsic fraud is held to be sufficient to vitiate an administrative order such as this, neither the pleadings nor the proof shows this to be a case of extrinsic fraud. *The fraud alleged here is the making of false statements* to the Railroad Commission. This type of fraud constitutes intrinsic fraud and for that reason would not be sufficient to vitiate the quasi-judicial ruling of the Commission. * * * Where an administrative agency acts in a judicial capacity on matters within its jurisdiction, as here, the decision made by the agency may not be attacked in a collateral proceeding on the ground of fraud. *Id.* at 487. [emphasis added; citations omitted]

This distinction has been accepted by the federal courts in reviewing agency actions. *United Merchants and Manufacturers, Inc. v. South Carolina Electric and Gas Com-*

pany, 113 F. Supp. 257, 262 (W.D. S.C. 1953), *aff'd*, 208 F.2d 685 (4th Cir. 1953); *see also United States v. Throckmorton*, 98 U.S. 61, 65-66 (1878).

II. UNDER SETTLED PRINCIPLES OF CORPORATE LAW, AN OFFICER AND DIRECTOR IS ENTITLED TO RELY UPON OUTSIDE EXPERT DETERMINATIONS IN THE EXERCISE OF BUSINESS JUDGMENT, AND HE CANNOT BE HELD LIABLE BY VIRTUE OF A POST HOC COLLATERAL ATTACK WHICH DISREGARDS SUCH DETERMINATIONS MADE BY AN AUTHORIZED STATE OFFICIAL.

This case goes to the very core concept of when an officer and director of a corporation may be held liable for breach of fiduciary duty. Here a corporate officer, director, and principal shareholder sought and received a ruling from the appropriate regulatory agency regarding valuation of an asset. He then undertook a program of acquisitions, in reliance upon that asset's valuation, and the acquisitions were also approved. He is now being held liable because the federal courts have seen fit to believe that the agency's determinations were erroneous. A most significant legal issue is therefore presented: is an officer and director of a regulated company justified in relying upon the regulatory agency's express determinations in making business decisions, or does he act at his peril?

Under the "business judgment" rule, it is well settled that an officer and director may take honest risks and not be liable even if the risk turns out badly. The rule has been well-summarized in a noted treatise:

> It is too well-settled to admit of controversy that ordinarily neither the directors nor the other officers of a corporation are liable for mere mistake or errors of judgment, either of law or fact. In other words, directors of a commercial corporation may take chances, the same kind of chances that a man would take in his own business. Because they are given this wide latitude, the law will not hold directors

> liable for honest errors, for mistakes of judgment, when they act without corrupt motive and in good faith, that is, for mistakes which may properly be classified under the head of honest mistakes. And that is true even though the errors may be so gross that they may demonstrate the unfitness of the director to manage the corporate affairs. This rule is commonly referred to as the "business judgment rule," which is generally applied to decisions of executive officers as well as those of directors. 3A W. Fletcher, *Cyclopedia of the Law of Private Corporations* § 1039 (1975).

In formulating a business strategy which may involve risks, upon what information or decisions may the director rely?

The Fifth Circuit held that the standard for fiduciary responsibility should be determined under Texas law. The Texas Business Corporation Act provides an absolute defense when a director has relied upon advice of counsel. Texas Business Corporation Act, art. 2.41(D) (1980). It also provides a defense under certain circumstances when the director has accepted the figures in the company's written financial statements based upon representations by accountants, or has considered assets to be of their book value. Texas Business Corporation Act, art. 2.41(C) (1980). However, no Texas statute or case specifies the standard for the defense of reliance upon expert advice in other contexts. The Model Business Corporation Act, upon which the Texas Act is based, is therefore highly persuasive in determining the common law standard in this case. After stating a general standard of care for directors, the Model Act provides that:

> In performing his duties, a director shall be entitled to rely on information, opinions, reports, or statements, including financial statements and other financial data, in each case prepared or presented by:
>
> (a) * * *

> (b) counsel, public accountants *or other persons as to matters which the director reasonably believes to be within such person's professional or expert competence* * * *
>
> (c) * * *
>
> but he shall not be considered to be acting in good faith if he has knowledge concerning the matter in question that would cause such reliance to be unwarranted. *A person who so performs his duties shall have no liability* by reason of being or having been a director of the corporation. *Model Business Corporation Act Annotated*, 270-71 (2d ed. 1977 Supp.). [emphasis added]

The official Comment to this section describes the scope of permissible reliance upon outside experts:

> As for reliance upon outside advisors, it is intended that there be included not only the professional disciplines customarily supervised by state authorities, such as lawyers, accountants and engineers, but also other fields involving special experience and skills, such as geologists, management consultants, and real estate appraisers. The concept of "expert competence" is intended to embrace a wide variety of qualifications and not be limited to the more precise and narrower recognition of experts under the Securities Act of 1933. *Id.* at 258.

Though there appear to be no Texas cases on point, the defense of reliance upon corporate records or advice of counsel has been recognized in jurisdictions such as New York and Delaware, in which corporate litigation is more frequent. *See, e.g., Graham v. Allis-Chalmers Manufacturing Co.*, 41 Del.Ch. 78, 188 A.2d 125, 130 (1963); *Gilbert v. Burnside*, 13 App.Div.2d 982, 216 N.Y.S.2d 430, 432 (1961). In applying state law, the federal courts have also recognized the need for directors to be able to rely upon independent determinations. Particularly, in the context of derivative suits, the business judgment rule

has been held to be an absolute defense to liability when independent directors, often in conjunction with outside experts, conduct an investigation and the directors rely thereon. *See, e.g., Burks v. Lasker*, 441 U.S. 471 (1979); *Lewis v. Anderson*, 615 F.2d 778, 781-83 (9th Cir. 1979); *Abbey v. Control Data Corp.*, 603 F.2d 724, 727 (8th Cir. 1979); *Maldonado v. Flynn*, 485 F. Supp. 274 (S.D. N.Y. 1980); *Rosengarten v. International Telephone and Telegraph Corp.*, 466 F. Supp. 817, 825 (S.D. N.Y. 1979). These cases have allowed reliance upon such independent determinations even when there has been a conflict of interest on the part of the directors, and even though the committee upon which the directors relied may not have been fully independent. The case for permitting reliance as a defense is therefore much stronger when a corporate director has relied upon a determination by a completely independent body (the state Insurance Department), and when no conflict of interest between the director and the corporation was present.

In fact, the director and the company have little choice in the matter. Under Texas law, the insurance company is required to obey an order of the State Board of Insurance until it is set aside upon a direct appeal. *Cosmo Life Insurance Co. v. State Board of Insurance*, 319 S.W.2d 162, 166 (Tex.Civ.App.—Austin, 1958). Of course, reliance by third parties can never be fully secure until any direct challenges have been completed. As one state court has recognized, where there is a statutory period in which to seek judicial review, "actions taken by other parties in reliance upon such order are taken at the risk that subsequently such order will be judicially disallowed in legal proceedings which are timely filed." *Stewart v. Martin*, 84 So.2d 235, 240 (La.Ct.App. 1955). But once the time for direct review has expired, are corporate officers still required to "act at their peril" in relying on such an order because ten years later the order might be collaterally attacked?

Since the company and its officers are required to obey administrative determinations, they should not be penalized for doing so. The federal courts have been sensitive to protecting persons who have relied on orders of state insurance commissioners during the period they are in effect. In *Preferred Risk Mutual Insurance Co. v. Manchester Insurance & Indemnity Co.*, 467 F.2d 1230 (7th Cir. 1972), an insurance company issued a policy endorsement limiting its risks, despite the fact that the Illinois Director of Insurance had ruled that the endorsement could not be used. The Seventh Circuit stated that "whatever the ultimate determination by the courts on the *prospective* use of the endorsement" in a direct challenge, the ruling must be given effect during the period it was extant. *Id.* at 1234. The court stated that it would be "inequitable" to retroactively apply a later court decision in a way which would injure those who had relied on the determination of the Director of Insurance.

If a director can rely upon counsel, outside experts, and committees, should he not be able to rely upon an expert and binding determination made by a state regulatory agency during the time it is in effect? There can be no doubt of the Insurance Commissioner's expertise. There is no contention that the assumptions upon which the valuation was based were more within Moody's knowledge than within that of the Commissioner. The past earnings of the shares in the life interest were a matter of record. Such matters as the appropriate discount rate to apply, the growth rate, and assumed annual income are essentially predictions about the future, which depend upon a wide variety of factors. They are the sorts of things with which insurance regulators deal all the time, and about which they must be assumed to have special expertise. When that expertise is exercised, and the adjudication binds the company, officers and directors may ignore it only at their own peril. It is perverse to hold that they *follow* it at their peril.

This central legal issue is disposed of by the Fifth Circuit in a footnote, for which no authority is cited. The Court stated:

> Moody also contends that, even if the $14,403,200 revaluation of the life interest were unreasonable, he is not responsible for Empire's subsequent losses because the Alabama Insurance Commissioner approved the revaluation. This contention is spurious. An insurance company may not delegate responsibility for valuation of its assets to a state agency, and the mere fact that an insurance commissioner accepts a company's asset valuation does not immunize the company from liability arising from that valuation. Pet.App. 22.

Petitioner has clearly shown that this unsupported "delegation" theory is contrary to Alabama state law. Pet. 12-13. It is also contrary to the law of Texas. In *Southwest Title Insurance Co. v. State Board of Insurance*, 390 S.W.2d 841 (Tex. Civ.App.—Austin, 1965), the issue in a direct appeal from a finding of the State Board of Insurance was: who had the power to value a major asset of the insurance company—the company itself, or the state agency? The Texas courts clearly stated that only the insurance regulators had that power:

> We do not believe that the [statute in question] permits companies to place their own valuation upon their assets, since other provisions of the Code *require* the Commissioner to examine such companies with respect to solvency, and if a company could fix its own valuation without proof, its capital could be impaired. *Id.* at 845. [emphasis added]

On the same page, the Court referred again to the "duty" of the State Board of Insurance regarding valuation of assets.

This is consistent with the legal theories prevailing in other states. The source of the insurance regulators' power and duty to make regulatory determinations does

not derive from a delegation by the company, but from a delegation of legislative power from the state legislature. *See, e.g., Hardware Mutual Casualty Co. v. Premo*, 153 Conn. 465, 217 A.2d 698, 705 (1966) (delegation of legislative power); *Kueckelhan v. Federal Old Line Insurance Company (Mutual)*, 69 Wash.2d 306, 418 P.2d 443, 452-53 (1966) (delegation by legislature); *Sims v. Manson*, 25 Wis. 2d 110, 130 N.W.2d 200, 202 (1964) (commissioner's powers are entirely statutory). If, as the Fifth Circuit contends, Moody had the power and duty to place his own valuation on the life interest, could he have ignored the decision by the Insurance Department in 1972 to reduce its value to $4,250,000—the decision which threw Empire into insolvency and receivership? If not, it is absurd to contend that the $14.2 million valuation arose from a "delegation" by Moody of his "responsibility" to value the life interest.

CONCLUSION

For the foregoing reasons, the petition for certiorari should be granted.

Respectfully submitted,

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